



**INTERNAL CONTROL RECOMMENDATIONS  
RELATED TO THE CASH THEFT AT THE LAND USE SERVICES –  
BUILDING & SAFETY DIVISION, VICTORVILLE OFFICE**

**Office of**

**AUDITOR/CONTROLLER-RECORDER**

# AUDITOR/CONTROLLER-RECORDER COUNTY CLERK



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November 29, 2007

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## SUBJECT: CASH AUDIT

### Introductory Remarks

In compliance with Article V, Section 6 of the San Bernardino County Charter and the Supervisor's Policy Statement 02-02 on Internal Operational Auditing, we have completed an operational audit on the Cash of Land Use Services. Our audit was conducted in accordance with the standards developed by the Institute of Internal Auditors.

### Background

The Department provides land use planning, building and safety, and code enforcement services to property owners within the unincorporated areas of San Bernardino County. As part of the services, permits are issued to build, alter, repair, move or demolish any building and to do electrical, plumbing, heating, solar, and air conditioning work. Permits may be obtained at local Building and Safety Division offices. Part of conducting business includes collecting fees for various demolition and construction permits. As a result, good cash handling controls are essential to protect the County and taxpayer assets. An audit report, Internal Control Recommendations Related to the Cash Theft of \$7,590 at the Land Use Services – Building & Safety Division, Victorville Office, dated May 9, 2006 and received by the Department on December 7, 2006, noted improvements needed for cash handling controls, at that office.

### Scope of Audit

The objective of this audit was to determine whether policies and procedures for cash handling and receipting were established and operating effectively during the period of 07/01/02-06/30/06. Specific audit objectives were to determine whether: cash on-hand equaled amounts entrusted to fund custodians; cash receipting practices effectively accounted for daily cash receipts; cash was safeguarded; and, supervisor oversight was effective. We conducted our audit according to the International Standards for the Professional Practice of Internal Auditing published by the Institute of Internal Auditors and

included tests of the accounting records, inquiries, and other procedures considered necessary. Also, we followed up on management actions for the audit report, Internal Control Recommendations Related to the Cash Theft of \$7,590 at the Land Use Services – Building & Safety Division, Victorville Office, dated May 9, 2006 and received by the Department on December 7, 2006. Our audit reviews were primarily conducted at the two full service offices at San Bernardino and Victorville.

A draft report was sent to the Department on October 26, 2007 and was discussed with management on November 29, 2007. The Department's responses to our recommendations are included in this report.

### **STATUS OF PRIOR YEAR'S FINDINGS AND RECOMMENDATIONS**

The following is the prior year finding that was still occurring as of 6/30/06:

#### **Finding 1 (Prior Year): Lack of internal controls**

The County of San Bernardino Internal Controls and Cash Manual (ICCM) requires each department to establish internal controls to safeguard cash.

A 2006 cash loss of over \$7,500 at the Department's Victorville Office resulted in an audit of cash handling controls at that office. The audit disclosed several cash handling controls deficiencies. As part of this audit, we reviewed the actions management had taken to resolve the control deficiencies noted in the audit.

Most deficiencies previously noted were resolved. However, although the safe had been moved, it was still in a location where the combination could be compromised when the safe is being unlocked.

#### **Recommendation:**

The Director of Land Use Services should move the Victorville office's safe to preclude compromising the combination when it is opened.

#### **Management's Response:**

LUSD Management disagrees with this assessment. As requested, the safe had been moved to a location that could ONLY be seen if someone were intentionally trying to observe the combination, and that person would be noticed by the employee opening the safe. However, in an abundance of caution attempting to solve ALL cash handling deficiencies in the Victorville

office, on February 6, 2007, LUSD Management assigned a full time Fiscal Specialist to a fully enclosed, locked office at that location. This position is now responsible for all cash handling duties, including the safe. The Fiscal Specialist reports to LUSD's San Bernardino Administrative staff. The enclosed office is kept locked when the employee is not available and the safe is not in view of other employees. Onsite backup is provided by the Building & Safety Supervising Land Use Technician for lunches and breaks. In the event the employee is out of the office for more than those time periods, a Fiscal Assistant or Fiscal Specialist from LUSD's San Bernardino Administrative staff is sent to the Victorville office to cover these duties.

**Auditor's Response:**

The Department's response addresses actions taken to correct deficiencies noted in the finding.

**CURRENT YEAR'S FINDINGS AND RECOMMENDATIONS**

**Finding 1: Lack of internal controls related to cash and checks**

The following did not comply with the *Standard Practice, Internal Controls and Cash Manual*:

1. During the cash reconciliation in the Victorville office, the supervisor did not count the cash receipts in the presence of the appropriate personnel—the supervisor counted the cash alone. It was noted that every time personnel receive cash they were instructed to log it and drop it in the safe—in some instances without proper verification of monies. Furthermore, there is not proper accountability of monies during the break or lunch of the fund custodian.
2. In San Bernardino, checks received in the mail are received by the receptionist and in turn given to the technicians. There is no evidence of transfer of custody of the checks from the receptionist to the technicians. The Department's cash receipting procedures do not require proper transfer thereby reducing accountability.
3. Staff in the Victorville office stated that the combination safe that secures the change fund for the Victorville Building and Safety Division had not been changed for over a year. In addition, management stated that the combination to the change fund's safe in San Bernardino had also not been changed for over a year. In addition, the Department does not keep a log keeping records of the dates the combination was changed.

Non-compliance with the Internal Controls and Cash Manual could result in lack of accountability of monies and leave the cash susceptible to misappropriation.

**Recommendation:**

The Director of Land Use Services should:

1. Add the requirement that all cash receipts must be counted in the presence of the appropriate personnel in accordance with the Internal Controls and Cash Manual to the Department's "Cash Deposit Procedures". In addition, train supervisors to provide proper accountability of monies when the fund custodian goes to break or lunch per the Internal Controls and Cash Manual.
2. Receipting procedures should be updated to reflect the requirement of proper transfer of monies.
3. Change safe combinations at least once a year or whenever there is a change in the staff that knows the combination, whichever is soonest. Maintain a log of combination changes showing the initials of the person documenting the change and the date the change occurred.

**Management's Response:**

1. a. Effective February 6, 2007, all cash receipts are now placed in a plastic pouch with a copy of the electronic receipt, after being counted in the presence of the Fiscal Specialist and the Land Use Technician, and then a cash log is filled out and initialed by both employees.  
b. If the Fiscal Specialist is not available, the Supervising Land Use Technician is given the cash and receipt and places them in the safe through a drop slot without unlocking the safe. When the Fiscal Specialist returns, she asks the Supervisor to return while she opens the pouch, counts the money, and the log is completed.
2. In the San Bernardino office the Receptionist logs the checks received by mail and gives them to the Supervising Land Use Technician and both employees initial the log. The Supervising Land Use Technician then distributes the checks to the appropriate Land Use Technician and they initial the log. Everyday, the Fiscal Specialist reviews the log to ensure that all checks have been processed.
3. The Administrative staff was changing the safe combinations as requested, but has begun keeping a log for verification purposes.

**Auditor's Response:**

The Department's response addresses planned actions as well as actions taken to correct deficiencies noted in the finding.

**Finding 2: Cash losses are not properly reported**

Per the *Standard Practice, Internal Controls and Cash Manual*, Chapter 5 pg. 5-3 and pg. 5-5, cash losses due to a cash handling error, fraud, theft, or embezzlement must be reported to the Internal Audits Section of the office of the Auditor/Controller-Recorder. \$702.11 of cash losses from four separate incidents during the period of 07/01/02-06/30/06 were taken from the cash receipts and a log of cash losses was not maintained. Management did not maintain a cash shortage log due to the small amounts of shortages.

Losses were not reported properly and therefore understated. In addition, since the losses were removed from the receipts, revenue was also understated. When losses are not reported, cash is susceptible to misappropriation.

**Recommendation:**

The Director of Land Use Services should maintain a log for cash handling shortages. In the event of a cash handling loss, the deposit should be made whole and any loss should be documented and taken from the change fund—not receipts. The log should be reviewed by management and appropriate action should be taken as stated in the ICCM including reporting the loss to the Internal Audits Section.

**Management's Response:**

All losses other than minor shortages in making change or customer payments that are received in the mail that are paid short have been reported to Risk Management but not always to Internal Audits. When a payment is received in the mail and is paid short, an attempt to contact the customer is made, provided the amount is material (over \$1.00). Otherwise the payment is accepted short and reported on the revenue recap. In the future, a log of all cash losses will be kept by the Administrative Manager and Supervising Fiscal Specialist. The new Supervising Fiscal Specialist is aware of the requirements and will be tracking and reporting all losses to Internal Audits on a monthly basis.

**Auditor's Response:**

The Department's response addresses planned actions as well as actions taken to correct deficiencies noted in the finding.

**Finding 3: Checks are not immediately endorsed**

Per the *Standard Practice, Internal Controls and Cash Manual* Chapter 3 pg. 3-3, checks must be endorsed immediately upon receipt. During the cash count in the San Bernardino and Victorville offices (Code Enforcement), the auditor noted that checks for the previous day's deposits were not immediately endorsed. Not immediately endorsing checks may allow them to be misappropriated more easily.

**Recommendation:**

The Director of Land Use Services should add the requirement to immediately endorse all checks after receipt to the Department's "Check Acceptance and Returned Checks (NSF) Policies". Furthermore, train employees on this process.

**Management's Response:**

Stamps were available to all Land Use Technicians who were reminded that it is required that all checks be immediately endorsed when received and verified as belonging to LUSD. Some checks received by this department do not belong to us and are then forwarded to the proper department or returned.

**Auditor's Response:**

The Department's response addresses planned actions as well as actions taken to correct deficiencies noted in the finding.

**Finding 4: Receipt books are not properly safeguarded and maintained**

Per *Standard Practice, Internal Controls and Cash Manual* Chapter 6 pg. 6-5, departments must keep a receipt control record indicating the receipt numbers received from Printing Services and the date issued to the cashier. Unused receipts on hand must be locked in a secure place where only one person has access to them. The Department's receipt log does not document the location where the receipt books were sent including the initials of the person recording the distribution. In addition, the log doesn't document if the

receipt book was returned by the cashier. Receipt books that are not properly maintained may be subject to misuse.

**Recommendation:**

The Director of Land Use Services should direct her staff to maintain a receipt control record indicating the receipt numbers received from Printing Services and when they are issued to or returned by cashiers.

**Management's Response:**

Since this department no longer issues full receipt books to staff, we stopped maintaining a log. When manual receipts were the department's only source for providing receipts to customers, a receipt log was kept. Electronic receipts are now used through the department's project and permit issuance system (Permits' Plus), and have been for several years, and include system generated numbers for tracking purposes. Also, the manual receipts this department has used for the last several years have been kept in a locked safe, are rarely used, and must be requested and signed for from the person responsible for the safe.

**Auditor's Response:**

Manual receipts are traditionally kept by departments to be used in case of a power or computer outage. These receipts can be used by Land Use Services staff to reassure customers that their payment was received. If these receipts are not controlled, the receipts can be incorrectly used to reassure customers while allowing the employee to avoid recording the transaction in the accounting system thus allowing a theft of the cash received. Prior to the audit, LUSD management had requested that all receipt books be returned to administration. However, during the audit of the Victorville Code Enforcement office, a blank receipt book was found in a drawer. LUSD administration was unaware of the non-returned book because the books were not logged as described within the management's response. This implies a lack of control over these receipts and therefore a risk of theft. To reduce this risk, LUSD staff should physically verify that there are no remaining unlogged receipt books. Only during a power or computer outage should the receipt books be removed from the safe and issued to cashiers. Periodically, but at least quarterly, the receipt books should be inventoried by someone above the custody of the books to verify that each receipt is intact.



**Finding 5: The Permits Plus Software System does not have proper security and cash controls**

Computer software systems must be protected to prevent unauthorized use. In addition, the rehearsal system should only be accessible during training. During the audit, the following conditions were noted:

1. The rehearsal system was easily accessible to all employees. In addition, the rehearsal system was able to generate identical receipts as the ones issued in the live system. Management did not verify transactions initiated through the rehearsal system. Because the rehearsal system transactions were not reviewed, funds could have been collected from and fraudulent receipts provided to customers.
2. The cash receipts report was used by the Department to reconcile cash receipts with offices within the Department. However, employees were able to enter receipt transaction data into the system without completing all of the stated required data fields, such as the location field. Since the cash receipt report was filtered through location identification number, if the employee forgot to put the location identification on the transaction, the transaction would not appear on the cash receipts report. Furthermore, receipt numbers listed on the cash receipts reports were not reconciled to verify that all receipt numbers were accounted for. This practice increases the risk of missing and possibly fraudulent transactions.
3. An employee at Victorville Code Enforcement was able to modify the customer name and address for transactions that had already been posted. Furthermore, the employee was able to print the modified transaction and issue another receipt with the new customer's information. In addition, the system doesn't track the modification made to the initial transaction. Management was not aware of this problem. This process increases the risk that monies may be subject to misappropriation.

**Recommendation:**

1. The rehearsal system must be uninstalled from all computers except those located in the training room. The training room should be kept secure at all times. After notification of the problem, the Department took immediate action and removed the software from all non-training room computers.
2. Require the transaction location identification field to be completed before the transaction can be posted. In addition, reconcile all receipt numbers

to ensure that all are accounted for. After notification of the problem, the Department took immediate action and changed the software specifications.

3. Do not allow any changes to be made to previously posted transactions. If changes are necessary, the transaction must be properly voided and a new transaction must be initiated. After notification of the problem, the Department took immediate action and changed the software specifications.

**Management's Response:**

While LUSD Management disagrees with findings 1 and 3 of this assessment, we took immediate steps to follow the advice of the audit team. LUSD staff did not understand the ability to generate fictitious receipts from the Permits' Plus "Rehearsal" module and was only able to change previously-posted transactions with specific directions from the audit team.

1. No one has the ability to access the rehearsal system and this was verified by the audit team.
2. A location identification field was always on the computer screen to be filled in but was not a required field. The department's IT staff has made this field a required field and payments cannot be accepted until it is entered.
3. Changes have NEVER been allowed to previously-posted transactions. Supervising Land Use Technicians or the Division Supervisors have always been required to void a transaction that required changes and are the only positions with void capabilities. On the printed report and receipt, the Permits Plus system only tracks the Land Use Technician employee number and not the supervisor who processed the void. However, the database does maintain this data, which can be reviewed by anyone.

**Auditor's Response:**

Due to LUSD management's immediate action to address the problems found by the auditor during the audit, the Department's response addresses actions taken to correct deficiencies noted in the finding.

**Finding 6: Petty Cash reimbursements are not in compliance with the Standard Practice Internal Controls and Cash Manual.**

The County of San Bernardino ICCM Chapter 4 requires each department to establish internal controls to safeguard cash. Part of the required controls

include: reimbursements must be approved by the immediate supervisor prior to the purchase of the item, and reimbursements must not exceed \$25 for services—unless written pre-approval is received from the Office of the Auditor/Controller-Recorder.

A review of 30 statistically selected transactions disclosed the following:

1. Fifteen reimbursement requests were either not accompanied by a Petty Cash Voucher or the receipt was not submitted for payment in its original form.
2. These same fifteen reimbursements were not accompanied by approval from the immediate supervisor prior to the purchase of the item.

The lack of supervisor oversight allowed the controls to be circumvented. Monies could be misappropriated due to non-compliance with the County cash manual regarding petty cash reimbursements.

**Recommendations:**

The Director of Land Use Services should ensure that all petty cash reimbursements are in compliance to the ICCM, and specifically ensure that:

1. Reimbursement requests are submitted with a Petty Cash Voucher and with their original receipts, and
2. Reimbursements are approved by the immediate supervisor prior to the purchase of an item.

**Management's Response:**

1. a. These fifteen petty cash payments were used for making payments related to monthly recurring expenditures such as telephone bills, subscriptions or other expenditures under \$25 and there would be no "original receipt" available and petty cash vouchers were not required by this department or County policy. The Auditor Controller-Recorder Accounts Payable section requires any payment under \$25 to be paid from petty cash and not through a payment request. The Administrative Manager will provide yearly written approvals for these payments.  
b. All other petty cash payments were required by this department to have a completed petty cash voucher and original receipts attached, which are on file with the payment document submitted to the Auditor/Controller-Recorder requesting petty cash reimbursement.

2. All Deputy Directors have been notified that any purchases made from petty cash must be accompanied by a written approval prior to the purchase being made. However, in some cases, such as disaster recovery efforts during the recent Slide and Grass Valley Fires, there isn't always enough time to obtain the proper prior written approvals. This department requests a written waiver from the Auditor/Controller-Recorder office exempting this department from this petty cash requirement during these emergency types of events.

**Auditor's Response:**

In item 1, the Department's response addresses planned actions taken to correct deficiencies noted in the finding. However, as requested in item 2, a waiver of the rules regarding supervisory preapproval of petty cash procedures cannot be given by the Internal Audits Section of the office of the Auditor/Controller-Recorder (ACR)—even in the case of emergencies. According to the Reimbursable Projects Section of the ACR, there is a Purchasing Liaison at the Emergency Operations Center during emergencies that expedites purchases during an emergency. This process, rather than petty cash, should be used for urgent items.

**Finding 7: Open permits are not being properly accounted for**

Per California Building Code 106.4.4, permits shall expire by limitation and become null and void if the building or work is not commenced within 180 days, or if the permit is suspended or abandoned at any time after the work is commenced for a period of 180 days. Any person holding an expired permit may apply for an extension of time for a period not exceeding 180 days. Presently, open permits are not being expired within the time limitations set forth in the building code. Furthermore, open permits are not accurately being updated as closed in the Department's Permits Plus software when the final inspection has been performed and the inspection record has been stamped finalized. Specifically,

- 6 out of 20 inspection's records reviewed showed inspections were not being performed within the criteria stated above and the permits remained open.
- 2 out of 80 permits reviewed showed final inspections were performed and stamped final but were not updated as closed in Permits Plus.

By not consistently reviewing permits and updating the permits for inspections performed, permits are not marked as expired that should be in a timely

manner. Open permits that should be marked as expired or closed within Permits Plus could overstate deferred revenue and/or understate earned revenue.

**Recommendation:**

The Director of Land Use Services should ensure that staff tracks building permits more accurately. If possible, they should perform an annual follow-up on all permits near their final stages of completion to ensure the permits are properly accounted for in the system. Also, ensure inspections are being performed every 180 days for each permit. Possibly, add a feature to Permits Plus that could flag any permits that are near the expiration date and review them to ensure they are in compliance with the code requirements.

**Management's Response:**

Due to a record increase in construction in the County of San Bernardino, LUSD has experienced an increased workload. During Fiscal Years 2004/05, 2005/06 and 2006/07, LUSD requested and the Board of Supervisors approved the addition of several Building Inspector positions. However, recruitment has been difficult and resulted in new staff that requires intense in house training and at least one year of field inspections to become proficient. Consequently, the increase in requests for inspections required LUSD to concentrate staff's efforts on active permits and inspections in order to provide quality customer service to those customers who are actively pursuing construction projects. LUSD understands the audit team's concern related to expired permits. However, it has always been this department's focus to work with their customers and provide as much flexibility as possible in order to help them succeed with their construction project. Many of our permits are issued to homeowners who complete their "weekend" projects over several years. This is a public service issue. Further, LUSD is in the process of implementing additional features of the Permits' Plus system that will allow for better tracking of expired permits and plans for this functionality to be complete by the end of the 2007-08 fiscal year. In addition, as construction within the County begins to slow, staff will begin reviewing all old permits, working with their customers, and determining the appropriate status of each permit.

**Auditor's Response:**

The Department's response addresses some planned actions taken to correct deficiencies noted in the finding. However, the auditor continues to be

concerned that deferred revenue and earned revenue could be misstated in the financial statements—particularly when a completed permit is not marked as such in the Permits Plus system. The Land Use Services department should focus their data input in this area and eventually begin updating expired permits as time permits.

**Acknowledgements**

We wish to thank the management and staff of Land Use Services for their assistance and cooperation throughout the audit.

Respectfully submitted,

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Auditor/Controller-Recorder

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